

## IC Armeec

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CLAIMS PAYING ABILITY RATING *	Update	Update
Date of Rating Committee:	16.12.2016	24.01.2018
Date of Publication:	19.12.2016	26.01.2018
Long-term rating:	BB+	BB+
Outlook:	stable	stable
National-scale long-term rating:	A- (BG)	A- (BG)
Outlook:	stable	stable

\* To become familiar with the full rating history, please, see the chart at the end of the document.

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**BCRA affirms the assigned ratings to IC Armeec:**

- Long-term claims paying ability rating: **BB+, outlook: „stable”;**
- Long-term national-scale rating: **A- (BG), outlook: „stable”.**

The methodology that BCRA has adopted officially is used for assigning ratings of the ability of insurance companies to pay claims ([http://www.bcrabg.com/files/file\\_202.pdf](http://www.bcrabg.com/files/file_202.pdf)).

To elaborate the credit report and to assign the credit rating, BCRA uses information from the rated insurance company, the FSC, the National Statistical Institute, its own database, consultants and other public information sources.

### Political Environment

With full EU membership in 2007, Bulgarian governments lose their main incentive to pursue a

reform policy. The country continues to be in a monitoring regime, with no significant progress in any of Bulgaria's problematic areas in the last years, which are mainly about fighting corruption and improving the functioning of the judiciary.

The complicated international situation also puts the country in serious trouble. The dependencies of a large part of the Bulgarian political and business elite from Russia and Turkey are evident. The war in Syria, on the other hand, puts Bulgaria at risk of a refugee wave. This strengthens nationalist and xenophobic attitudes, and the subject of refugees quickly finds place in political rhetoric.

Similar attitudes (nationalist and xenophobic) are also observed among EU member states. Some of them have a negative attitude towards the allocation of refugees by quota in each country and stand against this decision. If these disagreements get worse, they can lead to serious conflicts and division within the community.

### Economic Environment

In 2015, the economy reports a real growth of 3.6% – the highest value for the years after the financial crisis as among the main forces are domestic consumption and exports of goods and services. In 2016, the growth rate of economy slows down but remains close to the reported a year earlier – 3.4%, as among the groups with the largest contribution

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remains exports, and consumption of households and imports of goods and services slow down to half of the growth rates which the corresponding groups report in the previous year.

The flow of direct investments in the country doubles in 2015 (to 5.6% of GDP) compared to the reported in 2014 (2.7% of GDP). In 2016, Direct Investment Flows reduce (to 1.5% of GDP), as the investments in equity instruments come to barely 37.3% of the reported a year earlier, and the debt instruments continue to report a tide which triples compared to a year earlier.

The observed positive changes after 2013 in the labour market remain. With a descending trend in unemployment rate in the last three years, as of end-2016 the officially registered unemployment rate by the National Employment Agency reaches 8.0% (10.0% at the end of 2015) of the active population in the country. According to the data of the NSI (Labour Force Survey) unemployment rate of the population over the age of 15 years also follows this dynamics reaching 7.6% on average for 2016 compared to 9.2% for 2015.

The income on average for the economy increases in 2016 (up to 950 BGN/month), as nominal growth slows down (to 6.3%) compared to the reported a year earlier (8.8%), and the growth in average income over the year fluctuates between 9-10%.

Despite some slowdown in the decline of the prices in early 2016, in the second half and first 2 months of 2017, deflation remains at levels of about 1.1%-1.4% average annual, measured by HICP. The reasons for continuous deflation are due to changes in the prices of about half of the group of the index. Largest impact causes the changes in the group Transportation whose contribution fluctuates between 0.9-1.4 p.p. for April 2015 – February 2017.

#### Public Finance

A slight improvement is observed in the state budget of the country in 2015 that also continues in 2016.

Despite gradual growth in the state debt in the last three years, its stabilization at certain levels after March 2016 and restraint from issuing an external debt in the Budget Act for 2017 give grounds to expect a certain decline in its level in the current year. In addition, in 2017, three maturities take place, which are substantial by values (total 2.6

billion BGN) – the largest of which is on international capital markets programme (1.9 billion BGN). The level of the state debt continues to be a positive factor for Bulgaria (29.1% of GDP as of March 2016, as its level remains unchanged by the end of the year) compared to the EU indicators. The leverage, on average, for the EU is about 83.3% of GDP as of September 2016, and for the Eurozone it amounts to 90.1% of GDP. Only Estonia and Luxemburg stand before Bulgaria, respectively, by 9.6% and 21.5% of GDP as of September 2016, followed by Romania (36.2%) and Latvia (37.9%).

#### Banking system

On 13.08.2016 were disseminated the results from the conducted Asset Quality Review (AQR) and Stress Tests (ST) for stability of the banks in Bulgaria. The results show that the banking sector is stable, well capitalized and public support to banks with funds from the state budget is not necessary.

#### General insurance market in Bulgaria

The general insurance market in Bulgaria during the period of updating is characterized by:

- Strengthening the uptrend in written gross premiums income;
- High growth potential (in view of relatively low levels of insurance density and insurance penetration);
- High level of market concentration – in 2016 72.3% of Gross Premium Income (GPI) in the sector is formed by the seven largest companies (70.7% for 2015);
- High percent of motor insurances in the structure of aggregate insurance portfolio - 70.0% at the end of 2016 (68.4% at the end of 2015).

Main changes in the regulatory framework:

- In April 2016, the FSC adopted Ordinance (No. 51 of 28.04.2016) on own funds and solvency capital requirements of insurance and reinsurance undertakings, and groups of insurance and reinsurance undertakings;
- In December 2016, the FSC adopted Ordinance No. 53 of 23.12.2016 for the requirements of reporting, evaluation of assets and liabilities and formation of technical reserves of the insurance

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and reinsurance undertakings and the Guarantee Fund, and Ordinance No.54 of 30.12.2016 for the registers of the Guarantee Fund for exchange and protection of information and for the issuance and reporting of the compulsory insurances under Items 1 and 2 of Art. 461 of the Insurance Code;

- FSC had a session on 13.02.2017 and adopted Ordinance amending and supplementing Ordinance No. 13-41 of 12.01.2009 for documents and order for drawing them up in case of road traffic accidents and the procedure of communication between the Ministry of the Interior, the FSC and the Guarantee Fund;
- FSC had a session on 07.04.2017 and adopted Ordinance amending and supplementing Ordinance No. 49 of 16.10.2014 on the compulsory insurance pursuant to Items 1 and 2 of Art. 249 of the Insurance Code and on the Procedure of Settlement of Claims for Compensation of Damages Caused to Motor Vehicles.

The major factors hindering the development of general insurance companies continue to be slow recovery of the Bulgaria's economy from the crisis and low economic activity and determined by this insecurity with regard to future households revenues. The sector keeps high growth potential concerning relatively low levels of insurance density and insurance penetration.

*The results from the conducted Asset Quality Review (AQR) and Stress Tests (ST) of the insurance companies in the country published on 03.02.2017 bespeak for the stability of the rated company.*

There are no changes in subscribed share capital of IC Armeec during the period of updating and it remains in the amount of BGN 33 019 thousand. The majority shareholder remains CCB Group with a share of 84.47%. As a major priority in the company's development program for 2017-2018 is set improvement of the technical result in the car insurance through product development, a set of rules and procedures in signing and liquidation activities, etc.

Regarding Autocasco the company has undertaken portfolio's rehabilitation with the aim to decrease claims quota, including restrictions on risk clients, increase in premiums for hazardous brands, re-negotiation of price conditions, increased control over the signing process, etc.

The company holds Autocasco as the main business line in order to keep its leadership position, but the goal is a profitable business development and a gross claims ratio below 60%. The company has developed a strategic programme for balancing the portfolio by increasing its share and market position on property insurance.

In 2016, Gross premium income of IC Armeec declines by 12.2%, while on average for the sector there is growth of 3.1%. This reflects a market share loss of 1.94 p.p. to 11.26%. The main insurance Autocasco reports a decrease in the collected GPP of 3.0% (and consequently a loss of the market share of 2 p.p. on the insurance (up to 21.4%). More substantial are the losses for the other motor vehicle insurance Motor Third Party Liability, where the decline in GPP is 28.1%, and the market share reduces to 6.8% (10.0% in 2015). The decrease is due to the tariff and signing policy imposed by the insurance company. The reduction in the insurance portfolio in 2016 is determined by changes in the strategy and management principles of the company as the improvement in the technical result on business lines is a main priority in the company's management.

In the first half of 2017, GPP of IC Armeec increases by 4.2% on an annual basis, however, it lags behind the average for the sector (12.3%). As a result, there is again a loss of market share that reaches 10.88% (11.7% a year earlier). The collected GPP on the main insurance Autocasco reports an increase (1.3%) but despite this the market share of the company on the insurance reduces to 19.9% (21.5% a year earlier).

IC Armeec carries out active reinsurance, which however, decreases in the last periods: in 2016, GPP on active reinsurance is in the amount of BGN 328 thousand, compared to BGN 1,740 thousand. for the previous year, and in the first half of the year there is no realized GPP.

Regarding the structure of the insurance portfolio of the company in 2016, the uptrend retains in the share of Autocasco, which after 54.4% in 2015, in 2016 reaches 60.1%. At the expense of this, the weight of the other motor vehicle insurance Motor Third Party Liability continues to reduce, which reaches 23.2% (28.3% for 2015). In the first half of 2017, the uptrend in the share of Autocasco insurance has been interrupted and it decreases compared to 2016 (by 3.6 p.p.) and year-on-year (1.7 p.p.), reaching 56.5%. The share of the other

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motor insurance (Motor Third Party Liability) increases reaching 8.4% (5.5% a year earlier).

Regarding the comparison with the reference group composed of the other leading companies, IC Armeec continues to be characterized by a substantially higher level in the share of Autocasco insurance, while the share of Motor Third Party Liability remains significantly lower. Overall, the concentration in the company's portfolio is close to the average reported by the other leading companies.

In 2016, the gross claims ratio of IC Armeec remain almost without any changes compared to 2015 - 63.6% (62.9% in 2015), but net claims ratio increases by 10.7 p.p. reaching 55.9%. In the first half of 2017, the situation turns: gross claims ratio remain almost unchanged compared to the same period in 2016, while the net report a drop from 55.2% to 48.4%. Compared to the competitive group in 2016, IC Armeec reports a slightly higher size of net claims ratio, whereas in the first half of 2017, the company takes a more favorable position in comparative aspect.

The company continues to be characterized by lower levels of net acquisition ratio compared to the average for its direct competitors, which is a positive factor.

Unlike net acquisition ratio, expense ratio is kept at higher levels compared to the average for the competitive group.

In 2016, IC Armeec reports a level of combined expense ratio below 100% (97.1%), which is an indicator for realization of an insurance profit. At the end of the first half of 2017, however, the level of the indicator is above 100% (103.4%), which gives the company an unfavorable position in comparison with the other leading companies.

During the period of updating, the downtrend in the retention level of the company retains, i.e. IC Armeec continues to exceed an increasing share of the taken risks to reinsurers. In 2016, the reduction of the retention level is 10.78 p.p. to the level of 67.53%, and in the first half of 2017 – 7.42 p.p. compared to the respective period of 2016, to 61.34%.

In 2016, the volume of the investment portfolio of IC Armeec reports growth of 23.3% on a yearly basis after a decline of 0.7% for the previous year. The increase comes in line of almost all items with an exception of real estate which decrease by 7.8% and especially of deposits in banks which reduce

substantially – by 40.9% compared to the end of 2015.

In the first half of 2017, the size of the investment portfolio reports a decline of 10.2% compared to the end of 2016 (0.8% on a yearly basis). The share of the shares and stakes continue to rise reaching 59.4%. The volume of government securities decreases slightly by 1.5% compared to the end of 2016 and includes only Bulgarian government bonds. The deposits in banks continue to decrease – by 83.5% compared to the end of 2016, reaching barely 4 298 thousand BGN, which is 2.3% of the investment portfolio.

In 2016, the share of the high liquid assets of IC Armeec decreases insignificantly compared to the end of 2015. A more considerable decline is observed in the first half of 2017, when it reaches 24.3% (32.4% at the end of 2016), as this level continues to be substantially lower than the average for the adjusted sector<sup>1</sup>. The data shows that the investment income of IC Armeec retains strongly dominated by reevaluation of investment assets.

In 2016, IC Armeec reaches lower investment profitability than the average for the adjusted sector while in the first half of 2017 it slightly exceeds the average for the sector.

In 2016 the company realizes an insurance profit in the size of 4 257 thousand BGN, which is by 60.2% lower than the reported for 2015. The net profit is in the amount of 8 464 thousand BGN which is a decline of 11.5% on a yearly basis.

In the first half of 2017, the result of the insurance activity is negative, in the amount of BGN -1,928 thousand, while the net financial result amounts to BGN 1 911 thousand, which is by 63.3% less than the same period of the previous year.

During the last complete year, the company reports a decline in operating and financial leverage, but its levels remain higher than the average for the competitive group and the company continues to be unfavorably positioned. The reported liquidity levels of the technical provisions, the reserve for upcoming payments and the immediate liquidity are also unfavorable.

<sup>1</sup> Adjusted with the data of the rated company.

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### Main Financial Indicators

<b>Indicator / Year:</b>	<b>06.2017</b>	<b>06.2016</b>	<b>2016</b>	<b>2015</b>	<b>2014</b>
<b>Gross Premium Income (thousand BGN):</b>	<b>98 036</b>	<b>94 044</b>	<b>182 366</b>	<b>207 717</b>	<b>196 896</b>
<i>Change on a yearly basis</i>	4.2%	-48.4%	-12.2%	5.5%	11.0%
<b>Net Earned Income (thousand BGN):</b>	<b>56 695</b>	<b>81 366</b>	<b>147 456</b>	<b>172 614</b>	<b>175 698</b>
<i>Change on a yearly basis</i>	-30.3%	-44.8%	-14.6%	-1.8%	19.5%
<b>Net profit (thousand BGN)</b>	<b>1 911</b>	<b>5 211</b>	<b>8 464</b>	<b>9 569</b>	<b>-10 879</b>
Result from insurance activity	-1 928	5 172	4 257	10 689	-15 747
Gross Claims Ratio	64.7%	64.8%	63.6%	62.9%	71.7%
Net Claims Ratio	48.4%	55.2%	55.9%	45.2%	59.5%
Expense Ratio	40.9%	24.8%	25.8%	26.9%	26.5%
Acquisition Ratio	14.2%	13.6%	15.3%	21.8%	23.0%
Combined Ratio	103.4%	93.6%	97.1%	93.8%	109.0%
Operating Leverage	79%	126%	212%	291%	351%
Financial Leverage	254%	271%	263%	312%	438%
Liquidity Ratio	2.3%	6.4%	2.3%	2.7%	2.1%
Return on equity	7.6%	29.0%	13.1%	17.9%	-19.8%

### \*Rating History:

The ratings displayed in the chart are assigned under the previous Methodology for rating of the ability of insurance companies to pay claims, respectively with the applied rating scale and are not directly comparable with the ratings assigned after the entry into force of the current methodology on 04.07.2016.

<b>CLAIMS PAYING ABILITY RATING</b>	<b>Initial Rating 6.2006</b>	<b>Update 11.2007</b>	<b>Update 12.2008</b>	<b>Update 10.2009</b>	<b>Update 30.08.2010</b>	<b>Update 10.08.2011</b>
Long-term Rating:	BB+	iBBB-	iBBB-	iBBB	iBBB	iBBB
Outlook:	<i>stable</i>	<i>stable</i>	<i>stable</i>	<i>stable</i>	<i>stable</i>	<i>stable</i>
	<b>Update 10.08.2012</b>	<b>Update 14.10.2013</b>	<b>Update 07.11.2014</b>	<b>Update 06.11.2015</b>	<b>Update 05.07.2016</b>	
Long-term Rating:	iBBB	iBBB	iBBB	iBBB-	iBBB- (under review)	
Outlook:	<i>stable</i>	<i>stable</i>	<i>stable</i>	<i>stable</i>		